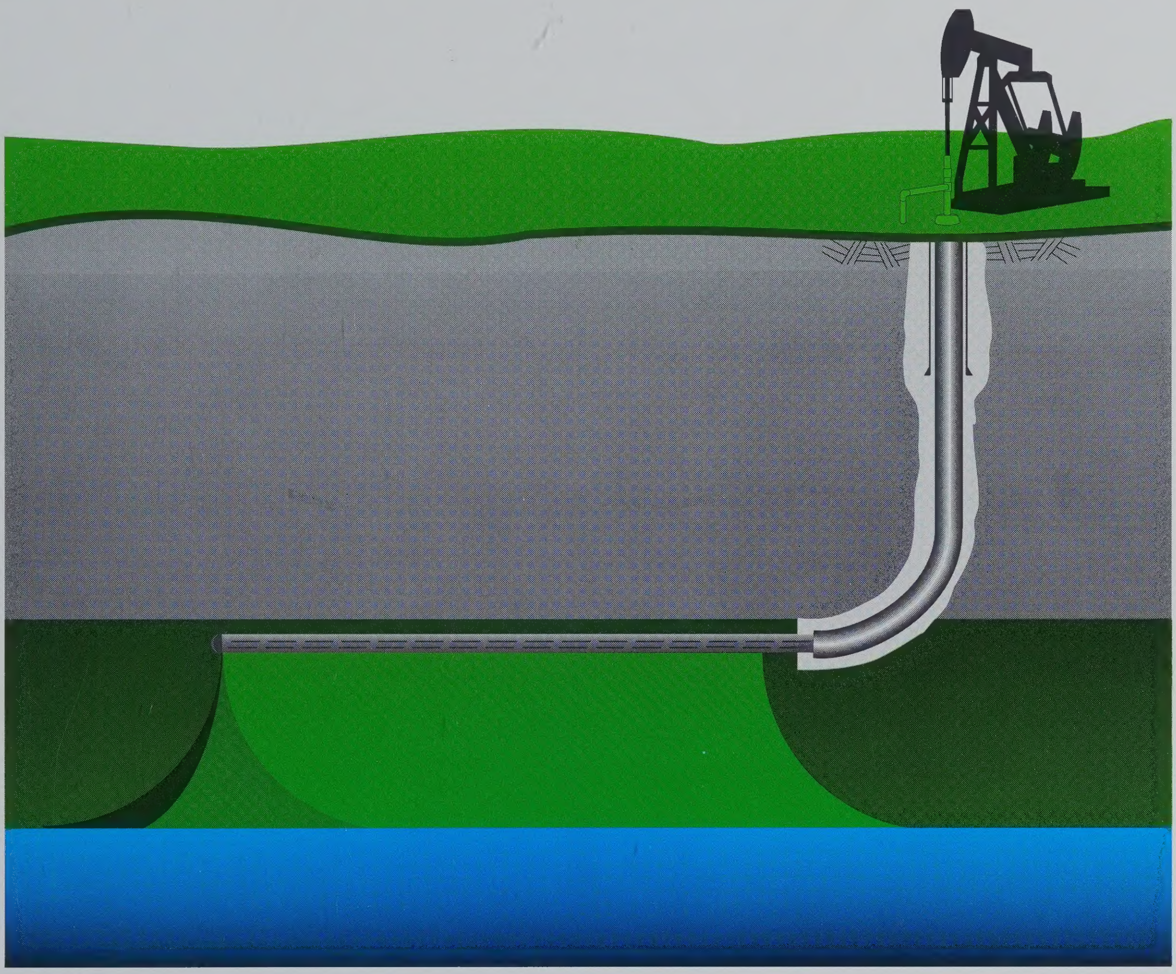

SOUTHWARD ENERGY LTD.

1992 ANNUAL REPORT

SOUTHWARD ENERGY LTD.

Corporate Information

Officers
Richard W. Kiser
President
Scott W. Kiser
Vice President and Secretary Treasurer

Directors
Richard W. Kiser
Scott W. Kiser
Gerald C. Saunders
Rick Ironside

Head Office
#330, 1201 - 5th Street S.W.
Calgary, Alberta
T2R 0Y6

Auditor
John Geib
Chartered Accountant
#331S - 8500 Macleod Trail South
Calgary, Alberta
T2H 2N1

Solicitors
Bennett Jones Verchere
Barristers and Solicitors
4500 Bankers Hall
855 - 2nd Street S.W.
Calgary, Alberta
T2P 4K7

Transfer Agent & Registrar
Montreal Trust
411 - 8th Avenue S.W.
Calgary, Alberta
T2P 1E7

Bank
Alberta Treasury Branch
420 - 2nd Street S.W.
Calgary, Alberta
T2P 3K4

Stock Exchange
Alberta Stock Exchange
300 - 5th Avenue S.W.
Calgary, Alberta
T2P 0L3

Trading Symbol
SWN

Front cover: Illustration adapted from horizontal well graphic, designed by Graham Ackerley of Morgan Hydrocarbons Inc.

To the Shareholders

The 1991 - 1992 fiscal period saw Southward book substantial reserve additions, decrease operating costs, increase revenues, and refocus corporate efforts toward crude oil reserves. These positive happenings have dramatically affected the future of the company.

During the year, Southward increased its reserve base by 80%, expressed in barrels of oil equivalent (BOE). Finding and development costs were exceptionally low at $2.34 per BOE. Operating costs were reduced to $2.74 per BOE versus $3.77 during 1990. Administrative costs were also reduced to $5.73 per BOE with a further reduction expected during the 1992 - 1993 fiscal year forecasted at $2.56 per BOE.

Petroleum and natural gas sales totalled $740,000, a 50% increase from the prior year. The dramatic effect of new sales and reduced operating costs, however, was achieved mainly in the fourth quarter of this past fiscal year. This positive impact is illustrated in the quarterly financial statements, enclosed with this report. Management is estimating that cash flow could reach 40 cents per share by Southward's year end in August, 1993.

Over the past few years, the Company has concentrated on developing natural gas prospects with an objective to fill contract requirements of 6 million cubic feet of gas sales per day. Throughout 1991, Southward assembled over 5000 acres of prospective gas bearing lands in Alberta by farmin and purchase at Crown land sales. In December 1991, the Company drilled a location on these lands based upon a prospective triple gas zone seismic lead. The successful well proved over 5 billion cubic feet of gas within the three prospective zones. This well, along with another Southward 100% owned shut in gas well, was placed on production during January 1992. These two wells, along with a third Southward well, are producing approximately 6 million cubic feet per day to the company's gas contracts. In May 1992, Southward constructed a gas compression facility for gas produced from these wells in order to avoid custom processing charges. Company compression is currently saving Southward approximately $30,000 per month in operating costs.

Upon fulfillment of Southward's gas contract needs, the directors determined that it was most prudent to diversify its product mix by defining and exploiting crude oil opportunities. With this objective, Southward obtained the consulting services of Mr. John Weston, an experienced and successful petroleum geologist. Mr. Weston identified several prospective Crown lands located in Southeast Saskatchewan. In March, June, and September of 1992, Southward purchased over 2700 acres of leases at Crown land sales with the objective of drilling

horizontal wells on the lands. Coincident with these operations Southward negotiated the purchase of $250,000 worth of oil production and facilities in the Moose Mountain area, in Saskatchewan. This purchase provided an initial three prospective drilling locations on the acquired lands. The first well on this lease was drilled in November 1992. Information on this well is provided in the Company's first quarter report.

Based upon the operations of this past year, the Company's directors have developed the following objectives for 1993:

1. Increase Company gas reserve base to at least ten billion cubic feet and add two million cubic feet per day of gas production.

2. Increase Company oil reserve base to at least one million barrels and daily oil production to a minimum of four hundred barrels per day (BOPD).

3. Achieve three million dollars annualized cash flow, while adding ten million dollars worth of proved oil and gas reserves to the company.

4. Raise one million dollars in capital funding.

5. Realize an increase in the trading value of Southward common shares as the above objectives are accomplished.

The foregoing objectives are attainable by implementing the corporate plan developed by your board of directors. The natural gas reserve base additions will be realized through a combination of drilling and acquisition. The oil reserve base additions will be accomplished through horizontal drilling on Southward lands in Southeast Saskatchewan.

Management is excited about the lower risk, high potential of its horizontal well locations in Saskatchewan. Southward will have participated in the drilling of three horizontal wells by the 1992 calendar year end. At the time of writing this report, two of these wells have been completed and have added over 50 BOPD to the company's production. Southward intends to operate and drill at least three additional horizontal wells by May 1993. We anticipate maintaining an average working interest approximating 50% in these wells after the payout of project costs. The wells drilled to date by the company have averaged an initial production capacity of 150 BOPD. With a 50% interest in the next three wells using our historical productivity average, Southward could realize 75% of its 1993 daily oil production objective by the end of its third fiscal quarter.

Management will be considering equity financing over the course of this coming year. Recently the federal government announced positive income tax changes

to flow through share funding. These new rules allow the issuing company to proceed with lower risk ventures using flow through share proceeds, while still providing the investors with 100% tax deductions on their share purchase price. This method of funding will be considered by the board as share prices increase.

It has been my experience in over thirty years in the petroleum industry that windows of opportunity occasionally occur. I have not seen a better time than the present for a junior resource company such as Southward Energy, to seize the best of many available opportunities. Our experienced team of explorationists and business people have dedicated their efforts to successfully manage the affairs of your company. We are excited with the challenge of the objectives we have set for the coming year. I invite our current shareholders, and all future shareholders, to follow the rapid growth of Southward Energy as we approach a new era of profitability.

On Behalf of The Board of Directors

RW Kiser

Richard W. Kiser - President

Auditor's Report

To the Shareholders of Southward Energy Ltd.

I have audited the balance sheet of Southward Energy Ltd. as at August 31, 1992 and the statement of operations and deficit and changes in financial position for the year then ended. These financial statements are the responsibility of the company's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the company as at August 31, 1992 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Calgary, Alberta
December 4, 1992

John J. Geib
Chartered Accountant

Balance Sheet

As at August 31, 1992

	1992	1991
Assets		
Cash	**$ 10,946**	$ -
Accounts receivable	**104,030**	58,805
Prepaids	**11,000**	-
	125,976	58,805
Capital (Note 2)	**2,123,180**	1,794,231
	$ 2,249,156	$ 1,853,036
Liabilities		
Bank Indebtedness	**$ -**	$ 356,720
Accounts payable and accrued	**201,454**	316,308
Convertible debentures	**-**	109,800
Long term debt (Note 3)	**324,000**	-
Capital lease (Note 4)	**67,830**	-
	593,284	782,828
Long term debt (Note 3)	**399,000**	-
Capital lease (Note 4)	**151,307**	-
Shareholders' Equity		
Share Capital (Note 5)	**1,896,815**	1,875,398
Deficit	**(791,250)**	(805,190)
	1,105,565	1,070,208
On Behalf of the Board	**$ 2,249,156**	1,853,036

Richard W. Kiser - Director

Scott W. Kiser - Director

Statement of Operations and Deficit

For the year ended August 31, 1992

	1992	1991
Revenue		
Petroleum and natural gas sales	**$ 739,492**	$ 488,964
Operators fees	**25,510**	12,001
Interest earned	**-**	2,620
	765,002	503,585
Royalties	**127,657**	64,255
	637,345	439,330
Direct Expenses		
Operating	**133,956**	82,782
Depletion and depreciation	**140,447**	119,500
	274,403	202,282
Revenue from Operations	**362,942**	237,048
Other Expenses		
Debenture interest	**30,708**	14,271
General and administrative	**281,867**	296,032
Interest and bank charges	**25,624**	41,518
Lease interest	**7,459**	-
Long term debt interest	**3,344**	-
	349,002	351,821
Income (loss) for the year	**13,940**	(114,773)
Deficit, beginning of year	**805,190**	690,417
Deficit, end of year	**$ 791,250**	$ 805,190
Basic earnings (loss) per share	**$.004**	($.03)
Fully diluted (loss) earnings per share	**$.003**	($.03)

Statement of Changes in Financial Position

For the year ended August 31, 1992

	1992	1991
Operating Activities		
Income (loss) for the year	$ 13,940	$ (114,773)
Item not requiring cash: Depreciation and depletion	140,447	119,500
	154,387	4,727
Net change in non-cash working capital balances related to operations	(171,081)	210,646
	(16,694)	215,373
Financing Activities		
Proceeds of debenture issuance	300,000	-
Proceeds of bank financing	750,000	-
Repayment of debentures	(409,800)	(18,000)
Repayment of long term debt	(27,000)	(79,978)
Net proceeds of share issuance	21,420	242,402
Proceeds of capital lease	228,300	-
Repayment of capital lease	(9,163)	-
	$ 853,757	144,424
Investing Activities		
Geological cost capitalized	(8,028)	(70,256)
Exploration and lease acquisition	(629,251)	(554,336)
Government grants	-	56,896
Proceeds of sale of petroleum and natural gas properties	172,967	60,000
Acquisition of office assets	(5,085)	(2,010)
	(469,397)	(509,706)
Changes in cash during the year	367,666	(149,909)
Cash at beginning of year	(356,720)	(206,811)
Cash at end of year	$ 10,946	$ (356,720)

Notes to the Financial Statements

1. Summary of Significant Accounting Policies

Southward Energy Ltd. is a publicly traded company engaged in the oil and gas business and is incorporated under the Alberta Business Corporations Act. These financial statements are prepared in accordance with generally accepted accounting principles, the more significant of which are:

a) Oil and Gas Operations

The company follows the full cost method of accounting in accordance with the guideline issued by The Canadian Institute of Chartered Accountants whereby all costs associated with the exploration for, and development of, oil and gas reserves, whether productive or nonproductive, are capitalized in cost centres. Such costs include land acquisition, drilling, geological and geophysical expenses related to exploration and development activities.

Gains or losses are not recognized upon the disposition of oil and gas properties unless such a disposition would change the depletion rate by 10% or more. Gains and losses are recognized upon the disposition of other assets.

Carrying values of oil and gas properties and share capital are reduced by grants received and transferred to flow through shareholders. Other grants earned under various government incentive programs are accrued and applied against the related expenditures.

b) Depreciation and Depletion

Furniture and fixtures are depreciated on a basis consistent with that used for capital cost allowance under the Canadian Income Tax Act. Tangible equipment, oil and gas properties and intangible are depleted on the unit of production method, based on proven reserves of oil and gas as determined by independent engineers and management's estimates. Natural gas reserves are converted to equivalent barrels of oil based upon the relative energy content of each product. In calculating depletion, gross proven reserves (before royalties) are used.

c) Ceiling Limitations

The net carrying value of the company's oil and gas properties is limited to an ultimate recoverable amount which is the aggregate of future net revenues from proved reserves and the costs of unproved properties net of impairment allowances, less future operating cost. Future net revenues are estimated using price escalation of 7% per annum (where warranted) discounted at a 15% present worth.

d) Income Taxes

The company accounts for income taxes by the tax allocation method, whereby income tax expense is determined as the amount that would be payable if statutory tax deductions for drilling, exploration and property acquisition costs and for capital cost allowances were claimed for tax purposes at the same rate as the related depletion and depreciation provisions charged against income.

e) Leases

Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incidental to the ownership of property is classified as a capital lease. At the inception of a capital lease, an asset and an obligation are recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair value at the beginning

of the lease. Assets recorded under capital leases are amortized on a unit of production basis over the estimated useful lives of the assets. All other leases are accounted for as operating leases wherein rental payments are expensed as incurred.

2. Capital Assets, at cost

	1992	1991
Obligation under capital lease	$ 230,600	$ -
Petroleum and natural gas properties	2,476,679	2,242,967
Furniture and equipment	59,194	54,109
	2,766,473	2,297,076
Less accumulated depletion and depreciation	643,293	502,845
	$ 2,123,180	$ 1,794,231

The company has unused cumulative Canadian oil and gas property expense of $159,376, cumulative Canadian development expense of $216,436, cumulative Canadian exploration expense of $895,003 and earned depletion of $42,487, available to reduce future taxable income.

3. Long term Debt

This amount represents a capital financing loan bearing interest at prime plus 1% per annum and is repayable in monthly instalments of $27,000 plus interest. A general assignment of book debts, a floating charge debenture of $250,000 and a fixed charge debenture of $400,000 are pledged as collateral against the debt.

Principal repayments over the next three years are as follows:

1993	$ 324,000
1994	324,000
1995	75,000
	$ 723,000

4. Capital lease

The company has a net obligation under a capital lease of $219,137 expiring in August 1995. The agreement bears interest at 10.37% per annum and requires blended monthly payments of $7,282. The company's compressor station is pledged as collateral against this debt. The company has assigned 19.45% of its interest in both the station and the lease to certain of the company's joint venture partners. The assignment was done at fair market value and the company remains contingently liable for the amount of the lease obligation assigned.

Principal repayments over the next three years are as follows:

1993	$ 67,830
1994	75,266
1995	76,101
	$ 219,137

5. Share Capital

	1992	1991
Authorized:		
20,000,000 common shares without nominal or par value		
Issued:		
4,054,940 shares (1991 - 3,914,923)	$ 1,896,815	$ 1,875,398

On January 1, 1992 stock options were issued in respect of 200,000 common shares exercisable at 15 cents per share. The options expire in four years and were granted to directors and an employee of the company.

On January 1, 1992 the company issued a one year share purchase warrant for 40,000 common shares at an issue price of 15 cents per share.

On January 1, 1992 the company issued a one year option for 10,000 common shares to a director of the company at an exercise price of 15 cents per share.

On June 4, 1992 certain directors and an employee exercised stock options in respect to 140,000 common shares for a value of $21,420.

6. Related Party Transactions

During the year the company paid remuneration to officers and/or directors or their nominees in the amount of $127,600 (1991 @ $122,400). Also, during the year two of the company's directors, along with third party industry partners, farmed in on one of the company's exploration projects. The interest earned by the directors and other parties will convert to one half of their participating interest upon payout of the project.

7. Subsequent Events

On September 10, 1992 the company issued stock options of 40,000 common shares to employees of the company. The options expire December 31, 1993 and are exercisable at 20,000 for 38 cents per share and 20,000 for 30 cents per share.

On October 1, 1992 stock options in respect of 40,000 common shares expired.

On October 8, 1992 warrants were exercised in respect to 280,000 common shares for a value of $112,000.

8. Income Tax

As August 31, 1992, the company had losses for income tax purposes in the amount of $90,586 which are available to reduce future years' taxable income. The loss expires in 1996.

PRINTED IN CANADA